The Centre for Philanthropy

Venimus, vidimus, clunes calcitravimus

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Submission to Treasury regarding the Draft Public Ancillary Fund Guidelines 2011.

1. Introduction

The Centre For Philanthropy is an Australian based organisation whose objects are the promotion of philanthropy especially in the areas of education, social welfare and health.

2. Summary of submission

We appreciate the opportunity to comment on the Draft Public Ancillary Fund Guidelines 2011 and hope that our submission and the submissions of others are seriously considered by Treasury.

According to clause 7 of the Guidelines "The object of these Guidelines is to set minimum standards for the governance and conduct of a public ancillary fund and its trustee."

While we broadly support the policy considerations dealing with transparency and accountability in operating a Public Ancillary Fund we believe the Guidelines as a whole are grossly overreaching and will significantly increase the red tape and cost of establishing and operating a Public Ancillary Fund resulting in a significant reduction in the use of a Public Ancillary Fund as a philanthropic tool. The Guidelines epitomise the 'nanny state' in the extreme.

A Public Ancillary Fund is nothing more than a conduit that receives money, property or benefits from the public that is distributed to a DGR listed in item 1 of Section 30-15. How complicated does its establishment and operation need to be?

Our particular concern is the restriction of people deemed to possess the qualities to be acceptable as trustees. The trustee qualifications greatly exceed those required of a company

director under the *Corporations Act 2001*. In addition we are unable to find any legal authority supporting the mooted '*responsible person'* requirements.

3. Submission

We will concentrate our discussion on clauses 14 and 14.1.

Clause 14 says;

> At all times, a majority of the individuals involved in the decision-making of the fund must be individuals with a degree of responsibility to the Australian community as a whole."
>
> Note 1: Those individuals with a degree of responsibility to the community as a whole are generally known as 'responsible persons'.

'Responsible person' is defined in Note 2 as:

> *'Individuals with a degree of responsibility to the Australian community as a whole' would generally include: school principals, judges, religious practitioners, solicitors, doctors and other professional persons, mayors, councillors, town clerks and members of parliament. Generally, individuals who are accepted as having a degree of responsibility to the community as a whole are known to a broad section of the community because they perform a public function or they belong to a professional body (such as the Institute of Chartered Accountants, State Law Societies and Medical Registration Boards) which has a professional code of ethics and rules of conduct. Individuals who have received formal recognition from the Government for their services to the community (for example, an Order of Australia award) will also usually have the requisite degree of responsibility*.

The definition in Note 2 is footnoted to the High Court of Australia case *Bray v Federal Commissioner of Taxation* (1978) 140 CLR 560. However, nowhere in *Bray* or for that matter any other case is there any mention that in order for a fund to qualify as a 'pubic fund' one or more trustees must be 'individuals with a degree of responsibility to the Australian community' nor is the term 'responsible person' used in any judicial context.

The 'responsible person' requirement appears to be an arbitrary bureaucratic policy developed for reasons of its own by the Australian Taxation Office which is now enunciated in Taxation Ruling 95/27. The classes of persons cited as having the requisite degree of 'responsibility' has no curial authority, in fact in the *Bray case* it was specifically pointed put that the public nature of a public fund had nothing to do with its management and control but derived entirely from the fact that the public contributed to it: see below. We can think of no reason on policy grounds why the many people who may be eminently suited to being trustees of public ancillary funds should be prevented from holding such a position simply because of the circumstance that they do not figure in list of 'responsible persons'.

We note that it is ironic that the protagonists in the *Bray* case would have qualified as 'responsible persons' under the proposals yet the case essentially involved tax avoidance by those responsible persons. On the other hand a member of the public who while as 'pure as the driven snow' would be excluded simply by the circumstance of their not being employed in one of the favoured professions or by a government body. In our view the acceptance by Treasury that people from a particular set of professions or occupying a government position are inherently possessed of greater integrity than 'ordinary' members of the public harks to a bygone age and ignores the plethora of scandals and frauds perpetrated everyday on the community by many people in those professions and government positions.

At the moment one of the acceptable classes of 'responsible person' is a director of a listed public company. To qualify as a director of a listed company the person in question must

simply be eighteen years of age and not disqualified under Part 2D.6 of the *Corporations Act 2001*. In other words there is an assumption that absent evidence to the contrary, any person over the age of eighteen is qualified to be a director of a listed company.

Academic and/or bureaucratic qualifications aside (an irrelevant factor when assessing a person's probity) the same can be said of all of the other categories of people deemed to be acceptable as responsible persons: no one is prevented from qualifying (or trying to qualify) for entry to those categories. Absence of academic qualifications or not working in a government position should not be a barrier to being accepted as a responsible person: many people, for example women who have looked after the family and home rather than pursue professional careers, at which they may have been spectacularly successful, in fields covered by the categories of responsible persons ought not be excluded from operating as a trustee of a Public Ancillary Fund simply by their circumstances.

Under the present arrangements, a person who would fail to be acceptable as a trustee of a Public Ancillary Fund could later become a director of a listed company and all of a sudden be qualified to be a trustee. In such a scenario there is no change in the qualifications of the person in question, merely a change in their circumstances. In our view it is unreasonable (and unwise) to exclude people from occupying positions where they can act for the public good simply on the grounds of circumstance. Thus if someone is qualified under section 201B of the *Corporations Act 2001* to be a director of a company, that is they do not fall within any of the disqualifying categories, they ought to qualify as a trustee of a Public Ancillary Fund.

The proposed legislation provides that the trustee of a Public Ancillary Fund must be either a constitutional company or Public Trustee of a State or Territory. However, the Guidelines set forth a standard for being a director of the constitutional company that would eliminate the vast majority of individuals who would otherwise qualify to be a director of a company under the *Corporations Act 2001.*

We submit that a similar test should be adopted by Treasury: that is the assumption should be that any person can be a trustee of a Public Ancillary Fund unless they would be disqualified under the *Corporations Act 2001.*

Such an approach would allow many people who wish to act as trustees of Public Ancillary Funds to do so when they would otherwise be disqualified as not falling within the current definition of 'responsible person'.

As stated earlier *Bray 78 ATC 4179; 140 CLR (19 May 1978)* makes no mention of any qualifications for trustees as a factor in determining whether a fund is a public fund.

Rather Barwick C.J said:

> There is no definition of a public fund provided by the Act: this is perhaps understandable because the circumstances which may warrant the conclusion that a fund is a public fund are likely to be various and quite disparate. But at least, in order for a fund to be a public fund, it must, in my opinion, either originate in a public initiative or attract public financial participation to a substantial degree. Given one of these conditions, there may yet be other circumstances which must be present to warrant the conclusion that the fund is of a public nature. In any case, a fund cannot obtain its public character from the nature of the purposes for which the fund may be used." (at p 4181)

Stephen J.I. concurs with J. Jacobs. (at p 4182)

Mason J said:

> "The fund established by the appellant under the trust deed which he executed was not in my opinion at any relevant time a public fund within the meaning of sec. 78(1)(a) of the Income Tax Assessment Act 1936 (as amended). It is not a sufficient qualification of a fund as a public fund that it is to be applied for public purposes. By insisting that the funds to which it refers shall be ``public" and at the same time specifying their purposes in such a way as to demonstrate that those purposes are to be public purposes the subsection requires that a fund in order to fall within the section shall have a public character distinct from the purposes for which it may be applied. See especially para. (iii), (v), (vii), (viii) and (xxxi) of sec. 78(1)(a).
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> "That the fund is open for subscription by the public is unquestionably an essential, though not in my opinion a sufficient, manifestation of its public character. It must also appear that the public participates in the fund by making contributions to it. No doubt the public character of the fund will be advanced by the participation of the public in its formation and in its administration but I cannot think that this is enough in itself without participation by the public in the making of contributions to the fund so as to constitute it as a public fund.
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> "In some cases it may be a nice question to determine whether the public has contributed to a fund. If the fund is, according to the terms of the instrument which constitutes it, open to subscription by the public then a comparatively few contributions by persons not associated with the settlor or promoter may be enough to satisfy the requirement of public participation, more particularly if the administration of the fund involves public participation. However, the present case is not a marginal case. The appellant was the sole contributor and the trustees were his friends and associates." (at p 4182)

The fact the other trustees were a barrister, accountant and solicitor was irrelevant.

Jacobs J said:

> A consideration of these circumstances leads me to conclude that the principal distinguishing characteristic of a public fund is that contributions thereto are sought from the public or a significant section of the public. If a member of the public contributes to such a fund as a result of an invitation or request so to do, that, it seems to me is positive, and probably irrefutable, evidence that the fund to which he contributes is a public fund and, if the purposes of the fund fall within sec. 78(1)(a), the contribution will be deductible."
>
> But what of the initial establishment of a public fund where the establishment is by an individual or a number of individuals? At that stage there is no contribution by a member of the public and perhaps no invitation to the public to contribute. Is it then necessary to examine the circumstances of the establishment of the fund or is it sufficient simply to examine the terms of the instrument under which the fund is established in order to ensure that contributions may be made to the fund by members of the public? If the latter be the correct view, then this fund qualifies as a public fund. If it is not correct, then it is necessary to determine what are the relevant circumstances."
>
> In my opinion it is not sufficient that the public under the terms of its establishment may contribute to the fund. That being so, it appears to me that it must be the intention of the promoters or of the founder or founders (if any) that the public will contribute so that in the case of a fund established by an initial gift from an individual or a few individuals what is born of the contribution from an individual or from individuals will blossom into a fund to which the public in fact subscribe. A fund is a public fund when the purpose of its establishment is the raising of funds from the public or a significant section of the public so that the objects will benefit to an extent greater than the benefit which a founder (if any) confers by his own contribution. The question is one of fact in each case and the conclusion would not be lightly reached that promoters or founders did not have the requisite intention or purpose. The fact that members of the public un-associated with the promoters or founders did in fact contribute in response to an invitation or request extended to them would no doubt be very strong evidence that the promoters or founders had extended the invitation to the public with the purpose intention and expectation that that result would follow." (at p 4187)

And per Aickin J:

> I am of opinion that the word ``public" in the phrase ``public fund" is used in the sense of being open to the public to make contributions to it. It is by way of contrast with ``private funds" which are open only to subscriptions by specified groups and not by the public generally. An appeal to the congregation of a particular church for subscriptions to a trust fund for the repair of the church, or a pension for a minister of that church, though charitable in the technical sense, would not be an appeal to the public or for a public fund. Similarly an appeal to former pupils of a particular school or to graduates of a particular university for subscriptions to a fund to be used for the benefit of the school or university would not be a public appeal, nor the fund resulting therefrom a "public fund".

Nowhere in the opinions of the learned Judges is there any mention that a factor in determining whether a fund is a 'public fund' is the qualifications of the trustees. The trustees in *Bray* were two solicitors, a barrister and an accountant yet the trust was found not to be a public fund because of the shenanigans involved in transferring the shares to the trust. The occupations and positions in the community of the trustees was totally irrelevant.

[*If anything Bray should establish that solicitors, barristers and accountants should not be trustees of public funds*.]

The citation to *Bray* in Note 2 of clause 14 of the Guidelines is an unequivocal and in our opinion appears to be an intentional misrepresentation of the ratio in the case. We find it difficult to believe that anyone educated in the law could read *Bray* and reach the conclusion that the case stood for the proposition that a majority of the trustees of a public fund must be individuals with a degree of responsibility to the Australian community as a whole and further that only the occupations stated in Note 2 and clause 14.1 qualify as such.

We strongly recommend that Treasury dispense with the notion of a class of qualifying 'responsible persons', for which there is no legal authority, and proceed on the assumption that unless disqualified by any particular factor such as those used in testing whether or not someone is a fit an proper person to be a company director, any member of the community possesses the attributes to be a trustee of a public ancillary fund. Such an approach aligns with both the philosophy inherent in the self-assessment regime and the presumption of innocence generally. There does not appear to be any reason on policy grounds why this approach should be resisted

We believe clauses 16 and 16.1 should be discarded because an individual would be disqualified from being a company director if convicted of a tax offence that is an indictable offence. These provisions are simply overkill.

B. MINIMUM ANNUAL DISTRIBUTIONS.

Over time these provisions will force a significant number of Public Ancillary Funds to dissolve. Requiring all Public Ancillary Funds to make the same minimum annual distribution discriminates against funds established in small markets. It is significantly more difficult to generate large amounts of donations in a small rural community or suburb of Perth, Brisbane, Adelaide, Hobart, etc. then in the large metro areas like Sydney and Melbourne.

If a group of individuals would like to establish a Public Ancillary Fund to support a community college and/or public benevolent institution in any rural or suburban

community it will be hard pressed to generate the donations necessary to meet the minimum annual distribution rules.

The fact that the amount of the minimum annual distribution itself is not net of expenses as described in the Note to clause 19 shows that Treasury has no idea of the amount of compliance costs Public Ancillary Funds are going to incur in meeting the requirements of the Guidelines.

C. EXPENSES

It appears Treasury has not costed out the expenses Public Ancillary Funds will incur to comply with the Guidelines.

1. Establishment cost.

2. Fundraising expenses as the public must be invited to contribute to the fund as required in clause 45.

3. Financial statements.

4. Audit.

5. Investment strategy. Considering very few if any of the occupations qualifying as 'responsible persons' would be qualified to prepare an investment strategy incorporating the requirements set forth in each state and territory trustee act the trustee would need to seek the advice of an outside investment firm to prepare an investment strategy.

   Of course the Investment Limitations set forth in clause 33 which are significantly more restrictive than those set forth in the various trustee acts will increase the cost of preparing and monitoring any investment strategy.

6. The cost for legal and accounting advice to comply with clause 48.

D. DONORS

We recommend that the language in clause 44 which footnotes *Bray* be removed as the responsible person requirement has no legal foundation as discussed above.

E. CONCLUSION

There are numerous deficiencies with the proposed Public Ancillary Fund Guidelines 2011 which will have far reaching implications for Public Ancillary Funds and philanthropy in Australia. We believe the Guidelines should be withdrawn and Treasury should consult with organisations such as The Centre For Philanthropy and others so that new Guidelines can be developed that will achieve the governments purported policy that Public Ancillary Funds comply with all relevant laws and obligations and are open, transparent and accountable to the public through the Commissioner.

However, if the underlying policy is to significantly reduce the number of Public Ancillary Funds established in the future and to cause many existing Public Ancillary Funds to dissolve then the Guidelines as written will achieve that policy.

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